



State of North Carolina

Office of the State Controller

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STATE CONTROLLER

STATE CONTROLLER RELEASES **2014 COMPREHENSIVE ANNUAL FINANCIAL REPORT**

December 8, 2014 – Contact: Sherri Johnson 919-707-0753

RALEIGH – The Office of State Controller (OSC) today released North Carolina’s 2014 Comprehensive Annual Financial Report (CAFR). The CAFR is prepared in accordance with generally accepted accounting principles.

North Carolina is one of the first states to complete and submit its CAFR. In fiscal year 2013, only four states (Michigan, New York, Utah, and Washington) submitted their CAFR prior to North Carolina’s submission. In addition, OSC received the Certificate of Achievement for Excellence in Financial Reporting by the Government Finance Officers Association of the United States and Canada (GFOA) for its 2013 Comprehensive Annual Financial Report. The award is the highest form of recognition in the area of governmental accounting and financial reporting. The 2013 award marked the 20th consecutive year that OSC’s CAFR received this noteworthy recognition. OSC believes the 2014 CAFR will meet or exceed the Certificate of Achievement Program requirements, and it has been submitted to the GFOA for review.

The CAFR is used by bond agencies and other financial organizations to assess the State’s fiscal health and economic outlook. During the 2013-14 fiscal year, the State issued general obligation and limited obligation refunding bonds. In connection with the refundings, Standard & Poor’s, Moody’s Investors Service, and Fitch Ratings, the top three rating agencies, all affirmed the triple-A bond rating for the State. The rating agencies recognized the State’s historically conservative budgeting, financial management, and debt issuance practices. North Carolina remains one of only 10 states with a triple-A rating from all three rating agencies.

The CAFR is prepared each year by the Office of the State Controller and audited by the Office of the State Auditor. The report, which outlines North Carolina’s financial condition, has received a “clean” opinion from auditors, indicating that it fairly represents the financial position of the State.

The full 2014 CAFR and a summary level Financial Highlights report based on the 2014 CAFR, are available on the OSC website at: www.osc.nc.gov.

Each year, OSC uses the cover of the CAFR to highlight the people, events and history of North Carolina. This year’s CAFR cover features the 2014 U.S. Open and the U.S. Women’s Open Championships hosted in Pinehurst, North Carolina. These two golf championships were held in back-to-back weeks (June 12 – 22, 2014), marking the first time in history that both tournaments were played in the same year, on the same course.

**STATE OF NORTH CAROLINA
KEY FINANCIAL RESULTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

General Fund

The General Fund is the chief operating fund of the State. The fund balance of the General Fund increased \$245.67 million (or 18.93%) to \$1.54 billion at June 30, 2014. The State collected \$452.6 million less in revenues than had been forecast, largely due to under collections in individual income taxes. The lower than expected individual income tax collections were partially offset by stronger than anticipated corporate income tax and sales and use tax collections. General Fund tax refunds, however, were significantly lower than the previous year. The improvement in the economy, as represented by the State's lower unemployment rate, has been shown historically to be related to lower refund ratios.

For fiscal year 2013-14, individual income tax decreased by 4.81% while sales and use tax and corporate tax revenues increased by 5.11% and 8.76%, respectively. The decrease in individual income tax was the result of changes to the North Carolina revenue laws that took effect for tax years beginning January 1, 2014. Prior to the 2014 tax year, the State individual income tax due was computed using a multi-tiered bracket system with tax rates of 6%, 7%, and 7.75%. Effective for the tax year beginning January 1, 2014, the State individual income tax rate is 5.8% for all individual income tax taxpayers in North Carolina. Individuals may no longer claim personal exemptions on the North Carolina individual income tax return, and many of the tax credits were repealed or expired. The growth in corporate income tax was due, in part, to a decrease in refunds. However, the growth in corporate taxes was partially offset by a decrease in the corporate tax rate. North Carolina revenue law changes reduced the corporate tax rate from 6.9% to 6%, effective for tax year January 1, 2014. Some of the increase in sales and use tax was attributable to North Carolina revenue laws that expanded the sales and use tax base, but most of the increase was due to improved economic conditions.

Highway and Highway Trust Funds

The fund balance of the Highway Fund decreased from \$343.99 million at June 30, 2013 (as restated) to \$214.87 million at June 30, 2014, a decrease of 37.53%. While the Highway Fund saw a higher increase in revenues than the previous fiscal year, expenditures still exceeded revenues resulting in a decrease in overall fund balance. Total revenues increased 7.89% to \$3.55 billion, mostly due to an increase in federal funds. An increased effort on closing and finalizing federal projects and billing of funds prior to expiration resulted in an overall increase in federal revenues. Total expenditures were \$3.49 billion, an increase of 2.77%. A focus on transportation infrastructure maintenance and preservation, including bridge preservation, contributed to this increase.

The fund balance of the Highway Trust Fund increased from \$609.23 million at June 30, 2013 (as restated) to \$878.12 million at June 30, 2014, an increase of 44.14%. The fund balance increase was primarily due to continued growth in new car sales which led to an increase in the highway use tax. Gasoline consumption also rose slightly from the previous year contributing to the overall increase. Total revenues increased 4.66% to \$1.18 billion, primarily due to the overall increase in the highway use tax. Total transportation expenditures were \$817.71 million, an increase of 7.6%. The initial phase of the Strategic Prioritization Funding Plan along with increased activity in both urban loop construction and secondary road construction contributed to the overall increase in expenditures for the year. The enabling legislation for the Highway Trust Fund also specifies that a designated amount will be transferred each year to the General Fund. The legislation was amended in 2008 to also require annual transfers to the N.C. Turnpike Authority to pay debt service or financing expenses for specified toll road construction projects (see Note 10(B) to the financial statements). The amount transferred to the General Fund for fiscal year 2013 was \$27.6 million. The budget legislation for fiscal year 2014 reduced the designated transfer amount to the General Fund to \$0.

Unemployment Compensation Fund

The Unemployment Compensation Fund (Trust Fund) reported net position of negative \$370.52 million at June 30, 2014 compared to negative \$1.56 billion at June 30, 2013. The improvement in net position is explained by 1) the drop in the State's unemployment rate from 8.8% in June 2013 to 6.4% in June 2014, 2) an additional increase in the Federal Unemployment Tax Act (FUTA) tax, and 3) the implementation of Session Law 2013-2. This law generated additional revenue by increasing state unemployment taxes on employers and decreased expenses by reducing the maximum weekly benefit amount and the maximum duration of unemployment benefits.

The Trust Fund's operating margin (operating revenues less operating expenses) was positive for the first time since fiscal year 2008, rising to \$1.02 billion this year compared to negative \$891.32 million in 2013. Employer unemployment contributions increased 9.72% to \$1.62 billion in 2014 due to increases to State (S.L. 2013-2) and Federal unemployment taxes on employers. Unemployment benefit expenses, both State and Federal, decreased 73.92% from \$2.43 billion in fiscal year 2013 to \$632.91 million in fiscal year 2014, due to claimants exhausting their maximum allowable benefits, a reduction in the number of new claimants, and the implementation of S.L. 2013-2. The amount owed to the federal government (that was advanced to finance State unemployment benefit payments) decreased 54.47% to \$980.99 million.

N.C. Education Lottery

As required by the enabling legislation, net revenues of the N.C. Education Lottery are transferred four times a year to the General Fund. The N.C. Education Lottery transferred \$503.14 million to the General Fund in 2014 to support educational programs for the State. The amount transferred in 2013 was \$478.51 million.

N.C. Turnpike Authority

The Triangle Expressway System, the State's first modern toll road, was constructed and opened in three phases. The third and final phase opened to toll traffic on January 2, 2013. The Triangle Expressway project, an 18.8-mile toll road, was delivered on schedule and under budget. Consequently, total operating revenues increased 83.16% to \$24.73 million primarily due to the increase in toll revenues. Sales of transponders peaked with the opening of the final phase in January 2013 and remained steady through the end of fiscal year 2014. The N.C. Turnpike Authority has completed the financing for the Monroe Connector System, a 20-mile toll road in Mecklenburg and Union counties. However, construction has been delayed due to litigation challenging the project's environmental documentation.

The gap between what tolling can pay for and the cost of the road requires additional support from the State, known as gap funding. The General Assembly enacted legislation authorizing annual transfers from the Highway Trust Fund to the N.C. Turnpike Authority to pay debt service and fund required reserves on bonds issued to finance turnpike projects. For fiscal year 2014, the N.C. General Assembly appropriated \$49 million annually for the Triangle Expressway and Monroe Connector projects.

Capital Assets and Long-term Debt

The State's investment in capital assets was \$45.64 billion, an increase of 3.93% from the previous fiscal year-end. The largest component of capital assets is the state highway system. North Carolina has a 79,578 mile highway system, making it the second largest state-maintained highway system in the nation. Significant year-end construction in progress amounts were for highway projects (\$1.61 billion), a toll road project (\$135 million), new psychiatric hospitals (\$203 million), and software development at the Department of Health and Human Services (\$248 million).

The State had total long-term debt outstanding (bonds, special indebtedness, and notes payable) of \$7.99 billion, a decrease of 7.1% from the previous fiscal year-end. The State issued \$506.26 million in refunding bonds to refinance previously outstanding general obligation and limited obligation bonds reported in governmental activities. The result is expected to be a decrease in future debt service payments of \$53.3 million.

The State Controller is North Carolina's chief fiscal officer. The Office of the State Controller serves as an independent resource to ensure the financial integrity of the State by providing accounting, disbursing, payroll, internal control, data management, eCommerce and financial reporting systems that serve state agencies, employees and the public and by maximizing financial return through its statewide cash management plan. OSC issues numerous financial reports including: General Fund Monthly Financial Report, IT Expenditures Report, Statewide Accounts Receivable Report, the State's Comprehensive Annual Financial Report (CAFR) as well as the short, easy-to-read CAFR Financial Highlights known as the "popular" report.